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## A Fair Slice for Developing Countries

Burgers, Irene; Mosquera, Irma

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- by [Irene Burgers](#) and [Irma Mosquera](#)
  - <http://www.austaxpolicy.com/fair-slice-developing-countries-policy-recommendations/>
- 



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At the time of writing, more than 100 countries are participating as Associates in the [Inclusive Framework on Base Erosion and Profit Shifting \(BEPS\)](#). More than 70 countries have signed a (binding) [Multilateral Instrument to Implement Tax Treaty Related Measures to Prevent BEPS \(MLI\)](#).

Despite developed and developing countries participating in these initiatives, the implementation of the BEPS Inclusive Framework and the MLI raises concerns on fairness. Some of the concerns – further highlighted in our Erasmus Law Review article ‘[Corporate Taxation and BEPS: A Fair Slice for Developing Countries?](#)’, will be addressed below.

In our view, governments, international organizations and researchers should pay more attention to what is meant by fairness in general, and to differences in perception between countries more specific in their discussions on how to prevent base erosion and profit shifting.

The OECD provided a definition of the principle of fairness in the [2003 Ottawa Taxation Framework Conditions](#), stating that: ‘this principle implies that the potential for tax evasion and avoidance should be minimized while keeping counter-acting measures proportionate to the risks involved’.

This definition was useful in the context of drafting the [BEPS Actions](#), but in our view, is too narrow in the BEPS implementation phase and thus should be redefined. Moreover, to make BEPS Actions successful in respect of developing countries, the international organizations and scholars should do follow-up work on the 2014 G-20 Development Working Group Report written by the Four International Organisations (IMF, UN, OECD and the WB, together ‘the Four IOs’) ‘[Options for Low Income Countries Effective and Efficient Use of Tax Incentives for Investment](#)’.

In this report, the Four IOs identify issues that have not been discussed in the BEPS project, which may result in tax base erosion or may reduce compliance such as:

- the use of tax incentives, which for developing countries are an essential tool to attract investors;
- the lack of technical and administrative capacity; and
- corruption.

In our view, fairness should not only be perceived from the legal perspective, but also from the economical perspective. Furthermore, in respect of the legal perspective, the definition should be given a wider scope, not only because developing countries may have a different perspective on what is fair legislation, but also because of differences in view on whether no more tax is due than what is required by the law or whether a fair share should be paid.

## **1. Different Economic Perspective of Fairness**

Developing countries have expressed in the [regional meetings](#) of the BEPS inclusive framework their need to maintain some of their tax incentives to attract investment. Although such incentives are often provided in a non-transparent ways and with a high degree of discretion, developing countries may perceive their tax system as being fair because to them this is the only way to be competitive.

Developed and developing countries also have different views on the allocation of taxing rights. This issue is more important since the allocation of taxing rights between residence and source has been left outside the scope of BEPS. Developing countries need to have a competitive treaty network if they are to implement all BEPS proposals and at the same time want to be able to attract foreign investment. The UN, for example, did not amend its [Model Tax Treaty](#) in line with the new Article 7 of the [2010 OECD Model Tax Treaty](#), which would result in loss of revenue and would complicate the allocation of profits to Permanent Establishments. The new Article 7 was adopted by the OECD following its [2008 Permanent Establishments Report](#) and it envisions taking into account dealings between different parts of an enterprise such as a permanent establishment and its head office to a greater extent than is [recognized](#) by the United Nations Model Convention. That approach by the OECD is now reflected in the new Article 7 in the 2010 OECD Model Convention and the Commentary on that Article. As stated in the UN Commentary to article 7, “the Committee of Experts decided at its 2009 annual session not to adopt the OECD approach to Article 7 arising from the OECD’s 2008 report Attribution of Profits to Permanent Establishments (the 2008 Permanent Establishments Report)”.

Developing countries also differ from developed countries in views about fair tax systems and efficient tax administrations. In response to a recognition that BEPS is a global problem, the African Tax Administration Forum (ATAF), organized a Consultative Conference on New

Rules of the Global Tax Agenda in Johannesburg, on 18 and 19 March 2014. In its [Discussion Paper](#), ATAF stated that,

in developing countries, beyond its fiscal role, the tax system has a more substantive role: it is an important tool for good governance and the basis for the social fiscal contract between governments and its citizens and corporations

The concerns of ATAF are important since these types of organizations are one of the three pillars of the OECD in translating the BEPS Action Plan into practical support for lower capacity developing countries.

ATAF's concerns in the context of "[The Global Tax Agenda and its implications for Africa](#)" show the BEPS Multilateral instrument and the BEPS Inclusive Framework should ensure that each participating country, including developing countries, benefits from BEPS, by raising more revenue, acquiring more technical expertise or by receiving a part of the revenue that the other country has obtained in part due to the efforts of the country. With developed countries cutting their development assistance budget after the recent global financial crisis, this has made developing countries realize that the achievement of the Millennium Development Goals (MDGs) and economic goals such as market reforms, promotion of private sector investment, industrialization and promotion of regional programs and development will depend heavily on domestic tax revenues. Consequently, creating robust and equitable domestic tax policies and implementing a fair and effective international tax system through international cooperation become primordial.

## **2. Differences in Juridical Perspective to Fairness**

In respect of the design of corporate income tax law, developing countries may have different ideas about equality compared to developed countries, especially where it concerns groups of companies. Tanzania, for example, from July 2012 [abolished](#) the participation exemption in Section 54(2) of the [Income Tax Act 2004](#), as it was considered not fair that contracts were not respected. Tanzania, like many other developing countries, for the same reason does not have a group treatment regime.

Developing countries generally also have different views on the juridical fairness of withholding taxes, not in the least for the economic reason that withholding taxes are simple and reliable sources of revenue. Often developing countries have high withholding taxes on passive income (dividend, interest and royalties).

Another difference on which developing countries may have other views than developed countries is legal certainty in terms of stability, promulgation, non-retroactivity and clarity of laws. The constant changes in legislation in developing countries results in less predictability and transparency, which can also affect the implementation of international tax standards such as BEPS. Developing countries do not yet have the same perception as developed countries on the relevance of providing legal certainty to taxpayers. Therefore, simple legislation is more important for developing countries, amongst others, due to the lack of sufficiently trained and sufficiently paid tax administrators and judges and also the lack of administrative guidance (such as rulings and concepts).

## **Recommendations**

The question will be what, if anything, can be done to achieve fairness for both developed and developing countries?

One issue which should be addressed in this discussion is the different perspective of different countries on whether the social contract theory underlies taxation and if so how the concept of 'fair share' could be made operable in such a way that it offers both taxpayer and the state sufficient certainty on the amount of tax to be paid. Academic research may offer some guidance into this.

We also recommend international organizations collectively work on following up the 2014 Report '[Options for Low Income Countries Effective and Efficient Use of Tax Incentives for Investment](#)' and the 2014 IMF Policy Paper, '[Spillovers in International Corporate Taxation](#)', to broaden the scope of the BEPS project accordingly. Comparative research by academic researchers may elevate the discussion to a higher level.

In light of the BEPS Agenda, further research should also be carried out on the implementation of BEPS in developing countries. The motivation for countries to participate and implement BEPS is not yet clear. It is also not clear how countries will implement BEPS including the role of the Legislative, Executive and Judiciary in the implementation, and whether the implementation of the BEPS Actions will be compatible with the rules to attract investment. Nor is clear how this implementation will influence the decision to invest by multinationals operating worldwide.

In order to achieve cooperation between states, we recommend that the UN should be included in the BEPS implementation. Notwithstanding the acknowledgment by developed countries of the leading role played by the OECD and the lack of resources in the UN, the UN should have a larger role in the discussion of BEPS with some additional financing by the World Bank. The UN has experience in the design of international tax proposals for developing countries. The UN also gives a voice to developing countries in the setting of international tax standards, which may lead to concrete proposals for cooperation between developing and developed countries. Therefore, the involvement of the UN is essential.

Furthermore, mechanisms for sharing extra revenue from BEPS measures between developing and developed countries should be included in the agenda of the BEPS Project. In order to address this issue, statistical information on the benefits and costs of BEPS should be collected either by the OECD or by academic researchers.

## **Final remarks**

Consensus on the meaning of fair taxation, both from an economical and legal point of view, is of utmost importance for a successful implementation of the BEPS Actions. In achieving such consensus, international organizations play an essential role, even if they do not have the same powers as legislators.

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